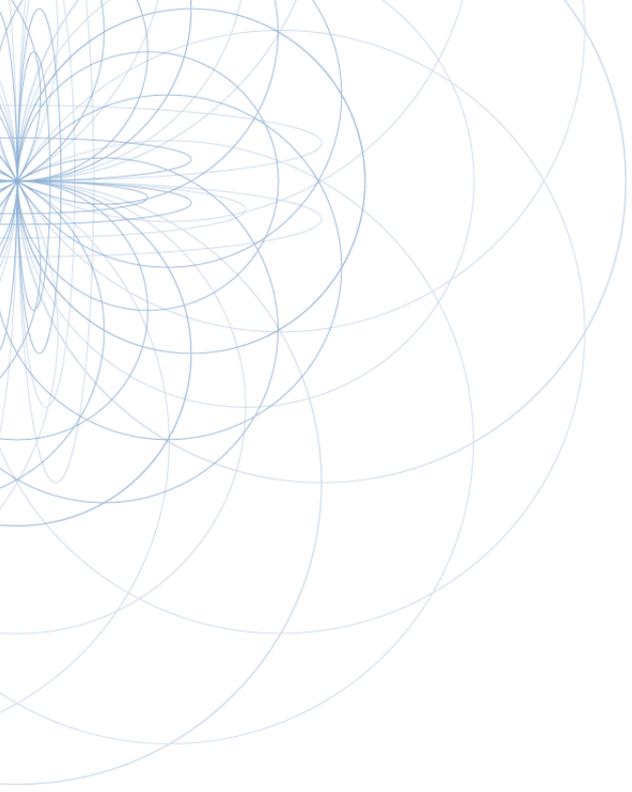


Financing of Funds Luxembourg



● **NautaDutilh** | Challenge the obvious

AVOCATS LUXEMBOURG



www.nautadutilh.com

This publication contains general information on current and upcoming legal issues and is not intended to be comprehensive or to constitute legal advice. It does not create a lawyer-client relationship. No rights whatsoever can be derived from this publication. NautaDutilh Avocats Luxembourg S.à r.l. is not liable for any damage which may arise as a result of any incorrectness or incompleteness of the information included in this publication. This publication does not suggest that NautaDutilh Avocats Luxembourg S.à r.l. or any of its lawyers are practising law of any jurisdiction other than Luxembourg. Should you require any legal assistance regarding any of the topics addressed herein, please contact NautaDutilh Avocats Luxembourg S.à r.l.

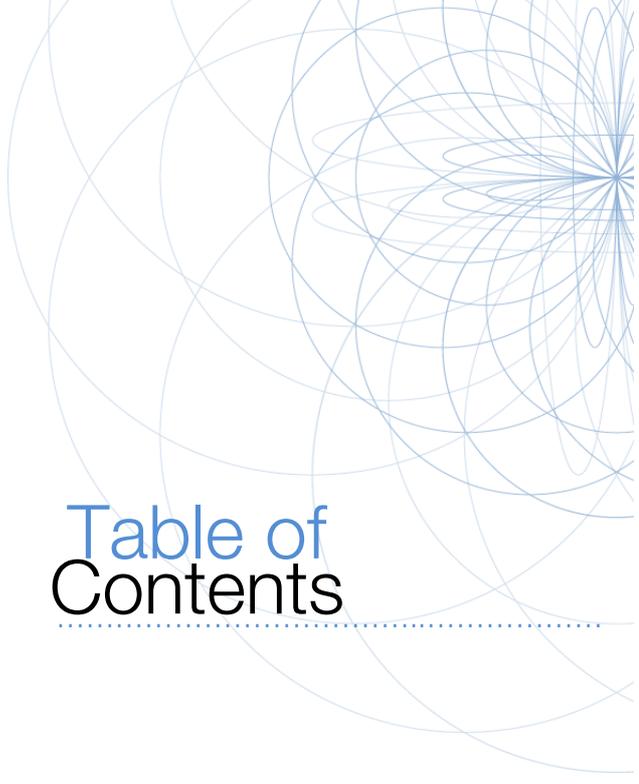


Table of Contents

1. Permitted Security	5
2. Permitted Leverage	6
3. Ranking	6
4. Regulatory Impact	7
5. Enhanced control of depositaries: a major concern for pledgees? ..	8
6. Conclusion	8
7. Contacts	9



What bankers and alternative investment fund managers should know about financing of Luxembourg alternative investment funds and Luxembourg regulated funds in general

The typical decisions banks and alternative investment fund managers (each an “**AIFM**”) must make when liabilities need to be secured by a collateral relate to aspects such as personal guarantee versus pledge or level of security taking. In addition, the following points need to be considered if the guarantor/pledgor is a regulated fund and/or an alternative investment fund (each an “**AIF**”).

1. Permitted Security

Generally, regulated funds (*i.e.* a specialised investment fund (the “SIF”), an undertaking for collective investment subject to the Part II of the UCI law (the “Part II Fund”) or an investment company with risk capital (the “SICAR”)) and/or AIFs may secure their liabilities by granting a security right over their assets. Banks as security takers prefer to use financial collateral arrangements under the Luxembourg Collateral Act to achieve this. A major advantage of the Collateral Act is that it offers insolvency remoteness. This means that a security right does not run any risk of being invalidated by an insolvency official, even if it has been granted during the hardening period. A financial collateral arrangement is effective following minimal formalities. It can be enforced without any prior court order.

The type of security or the ability to grant such security may be limited by the corporate documents of the relevant entity and/or the law applicable to such entity.



2. Permitted Leverage

The permitted leverage of AIFs will depend not only on applicable fund/fund manager regulations and regulatory practice but also on any borrowing restrictions embedded in its fund documents, including the fund prospectus / private placement memorandum (the “PPM”).

Given the many types of regulated funds and AIFs existing under Luxembourg law, leverage restrictions may vary for each regulated fund, typically going from 25% up to 75% of the fund’s net asset value.

As lenders cannot be sure about the AIF’s current debt commitments, they will usually ask for a confirmation on the level of undertakings/outstandings.

If several compartments are set-up within one fund/AIF, a loan taken by one compartment does not in principle trigger cross-obligations towards any other compartment of the same umbrella fund/AIF. Luxembourg law indeed provides for the possibility to ring-fence the assets and liabilities of the umbrella’s various compartments so that the creditors of another compartment may not have any recourse against the assets of the relevant compartment to which a loan is granted. Therefore, permitted leverage is usually measured at compartment level.

3. Ranking

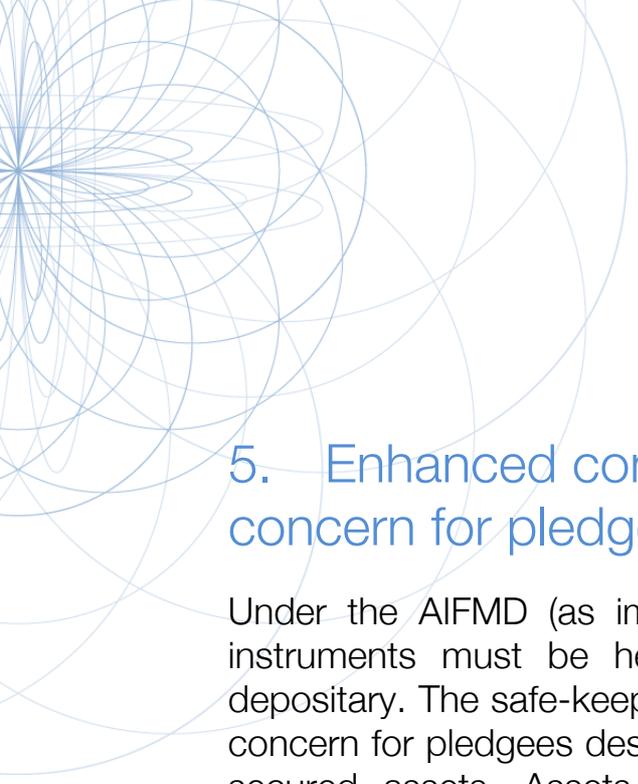
Where banks, acting as pledgees, benefit from a collateral, they will rank ahead of the fund/AIF’s limited partners/shareholders. The investors’ attention to this fact is in principle drawn in the PPM prior their making a decision to subscribe to interests/shares in a fund/AIF (or compartment thereof).

4. Regulatory Impact

An AIFM managing one or more AIFs, one of which (including a compartment thereof) having entered into a loan financing agreement with a bank, or providing a security in favour of the bank in relation to a loan granted to an affiliate or target, will be subject to the full scope of the alternative investment fund manager Directive and related implementing measures (the “AIFMD”) from a lower threshold of assets under management (*i.e.* EUR 100 million instead of EUR 500 million (for unleveraged AIFs with no redemption right during 5 years following subscription)).

Furthermore, bridge facilities may, subject to a couple of criteria, be excluded from the leverage notion so that the higher threshold may apply.

Therefore, deciding on type and level of leverage may be of strategic importance for smaller AIFMs not only from a performance standpoint but also from a regulatory angle.



5. Enhanced control of depositaries: a major concern for pledgees?

Under the AIFMD (as implemented in Luxembourg), AIF's financial instruments must be held in custody with a Luxembourg-based depositary. The safe-keeping obligations of the depositary may raise a concern for pledgees desirous to keep a maximum of control over the secured assets. Assets which are not financial instruments shall remain under the depositary's control based on ownership verifications and adequate record keeping.

Therefore, the content of the pledge agreement and the depositary agreement must be aligned and solutions on minimising the potential negative impact of control of the depositary for the pledgee are to be negotiated on a transaction-per-transaction basis.

6. Conclusion

The setting-up of parallel financing in addition to equity injections requires adequate legal structuring and the consideration of securities and regulatory laws aspects.

7. Contacts

For any questions, please contact us at NautaDutilh Avocats Luxembourg S.à r.l., we are pleased to assist you.



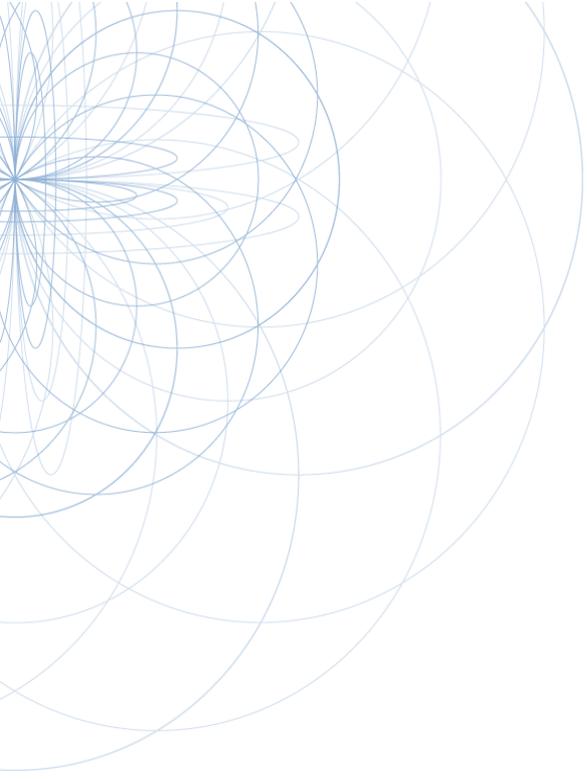
Josée Weydert
Banking & Finance Partner
T. + 352 26 12 29 97
E. josee.weydert@nautadutilh.com



Ezechiel Havrenne
Investment Funds Partner
T. + 352 26 12 29 7409
E. ezechiel.havrenne@nautadutilh.com



Jad Nader
Banking & Finance Counsel
T. + 352 26 12 29 63
E. jad.nader@nautadutilh.com



Challenge
the
obvious